MERCER INTERNATIONAL INC.
Form 10-Q
July 28, 2016

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

# FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended June 30, 2016**

**OR**

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the transition period from __________ to __________**

**Commission File No.: 000-51826**

**MERCER INTERNATIONAL INC.**

**(Exact name of Registrant as specified in its charter)**

| | |
|---|---|
| **Washington** | **47-0956945** |
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer Identification No.)** |

**Suite 1120, 700 West Pender Street, Vancouver, British Columbia, Canada, V6C 1G8**

**(Address of office)**

**(604) 684-1099**

**(Registrant s telephone number, including area code)**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the *Securities Exchange Act of 1934* during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO ¨

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months or for such shorter period that the registrant was required to submit and post such files). YES x NO ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

| | | | |
|---|---|---|---|
| Large Accelerated Filer | x | Accelerated Filer | ¨ |
| Non-Accelerated Filer | ¨ | Smaller Reporting Company | ¨ |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO x

The Registrant had 64,694,138 shares of common stock outstanding as at July 27, 2016.

# PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## MERCER INTERNATIONAL INC.

## INTERIM CONSOLIDATED FINANCIAL STATEMENTS

## FOR THE SIX MONTHS ENDED JUNE 30, 2016

**(Unaudited)**

**MERCER INTERNATIONAL INC.**

**INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS**

**(Unaudited)**

**(In thousands of U.S. dollars, except per share data)**

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | **2016** | **2015** | **2016** | **2015** |
| Revenues | | | | |
| Pulp | $ 198,055 | $ 246,126 | $ 428,684 | $ 480,783 |
| Energy and chemicals | 20,090 | 20,810 | 43,304 | 43,700 |
| | 218,145 | 266,936 | 471,988 | 524,483 |
| Costs and expenses | | | | |
| Operating costs, excluding depreciation and amortization | 173,227 | 205,293 | 370,169 | 390,241 |
| Operating depreciation and amortization | 17,855 | 16,393 | 34,887 | 33,697 |
| Selling, general and administrative expenses | 10,286 | 11,701 | 22,055 | 23,065 |
| Operating income | 16,777 | 33,549 | 44,877 | 77,480 |
| Other income (expenses) | | | | |
| Interest expense | (12,736) | (13,476) | (25,927) | (27,360) |
| Foreign exchange gain (loss) on intercompany debt | (272) | 2,198 | 283 | (4,412) |
| Other income (expenses) | (137) | 68 | (633) | (470) |
| Total other expenses | (13,145) | (11,210) | (26,277) | (32,242) |
| Income before provision for income taxes | 3,632 | 22,339 | 18,600 | 45,238 |
| Current income tax provision (Note 6) | (3,372) | (3,149) | (5,125) | (6,501) |
| Deferred income tax provision (Note 6) | (4,501) | (2,778) | (8,947) | (8,691) |
| Net income (loss) | $ (4,241) | $ 16,412 | $ 4,528 | $ 30,046 |
| Net income (loss) per common share (Note 8) | | | | |
| Basic | $ (0.07) | $ 0.25 | $ 0.07 | $ 0.47 |
| Diluted | $ (0.07) | $ 0.25 | $ 0.07 | $ 0.46 |
| Cash dividends declared per common share (Note 7) | $ 0.115 | $ | $ 0.23 | $ |

**INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

**(Unaudited)**

**(In thousands of U.S. dollars)**

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | **2016** | **2015** | **2016** | **2015** |
| Net income (loss) | $ (4,241) | $ 16,412 | $ 4,528 | $ 30,046 |
| Other comprehensive income (loss), net of taxes | | | | |
| Foreign currency translation adjustment (net of tax effect of $nil in all periods) | (26,981) | 31,045 | 25,355 | (80,760) |
| Change in unrecognized losses and prior service costs related to defined benefit plan (net of tax effect of $nil in all periods) | 289 | 211 | 579 | 459 |
| Change in unrealized gains/losses on marketable securities (net of tax effect of $nil in all periods) | 4 | (7) | 2 | (78) |
| Other comprehensive income (loss), net of taxes | (26,688) | 31,249 | 25,936 | (80,379) |
| Comprehensive income (loss) | $ (30,929) | $ 47,661 | $ 30,464 | $ (50,333) |

*The accompanying notes are an integral part of these interim consolidated financial statements.*

**MERCER INTERNATIONAL INC.**

**INTERIM CONSOLIDATED BALANCE SHEETS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| **ASSETS** | | |
| Current assets | | |
| Cash and cash equivalents | $ 112,651 | $ 99,629 |
| Restricted cash (Note 10) | 7,834 | 9,230 |
| Accounts receivable | 125,384 | 134,254 |
| Inventories (Note 2) | 134,847 | 141,001 |
| Prepaid expenses and other | 5,048 | 4,697 |
| Total current assets | 385,764 | 388,811 |
| Property, plant and equipment, net | 767,014 | 762,391 |
| Intangible and other assets | 8,603 | 8,461 |
| Deferred income tax | 18,888 | 23,154 |
| Total assets | $ 1,180,269 | $ 1,182,817 |
| **LIABILITIES AND SHAREHOLDERS EQUITY** | | |
| Current liabilities | | |
| Accounts payable and other (Note 3) | $ 103,495 | $ 103,450 |
| Pension and other post-retirement benefit obligations (Note 5) | 1,033 | 971 |
| Total current liabilities | 104,528 | 104,421 |
| Debt (Note 4) | 616,492 | 638,043 |
| Interest rate derivative liability (Note 10) | 2,898 | 6,533 |
| Pension and other post-retirement benefit obligations (Note 5) | 26,562 | 25,374 |
| Capital leases and other | 11,981 | 12,299 |
| Deferred income tax | 17,588 | 13,171 |
| Total liabilities | 780,049 | 799,841 |
| Shareholders equity | | |
| Common shares $1 par value; 200,000,000 authorized; 64,694,000 issued and outstanding (2015 64,502,000) | 64,656 | 64,424 |
| Additional paid-in capital | 330,669 | 329,246 |
| Retained earnings (Note 7) | 150,533 | 160,880 |

| | | | | |
|---|---|---|---|---|
| Accumulated other comprehensive loss (Note 9) | | (145,638) | | (171,574) |
| Total shareholders equity | | 400,220 | | 382,976 |
| Total liabilities and shareholders equity | $ | 1,180,269 | $ | 1,182,817 |
| Commitments and contingencies (Note 12) | | | | |
| Subsequent event (Note 7) | | | | |

*The accompanying notes are an integral part of these interim consolidated financial statements.*

**MERCER INTERNATIONAL INC.**

**INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(Unaudited)**

**(In thousands of U.S. dollars)**

| | Three Months Ended June 30, 2016 | Three Months Ended June 30, 2015 | Six Months Ended June 30, 2016 | Six Months Ended June 30, 2015 |
|---|---|---|---|---|
| Cash flows from (used in) operating activities | | | | |
| Net income (loss) | $ (4,241) | $ 16,412 | $ 4,528 | $ 30,046 |
| Adjustments to reconcile net income (loss) to cash flows from operating activities | | | | |
| Depreciation and amortization | 17,962 | 16,483 | 35,181 | 33,870 |
| Deferred income taxes | 4,501 | 2,778 | 8,947 | 8,691 |
| Foreign exchange (gain) loss on intercompany debt | 272 | (2,198) | (283) | 4,412 |
| Defined benefit pension plan and other post-retirement benefit plan expense | 398 | 385 | 874 | 1,094 |
| Stock compensation expense | 764 | 728 | 1,655 | 1,358 |
| Other | 33 | 288 | 1,259 | 1,268 |
| Defined benefit pension plan and other post-retirement benefit plan contributions | (458) | (438) | (884) | (913) |
| Changes in working capital | | | | |
| Accounts receivable | 8,548 | (13,061) | 12,501 | (22,682) |
| Inventories | (3,648) | (727) | 10,988 | (5,648) |
| Accounts payable and accrued expenses | (13,313) | (9,702) | (103) | 18,071 |
| Other | 459 | (514) | 80 | 712 |
| Net cash from (used in) operating activities | 11,277 | 10,434 | 74,743 | 70,279 |
| Cash flows from (used in) investing activities | | | | |
| Purchase of property, plant and equipment | (13,479) | (11,707) | (20,415) | (18,771) |
| Purchase of intangible assets | (416) | (1,017) | (936) | (1,890) |
| Decrease in restricted cash | 1,595 | | 1,595 | |
| Other | 849 | 75 | 747 | 297 |
| Net cash from (used in) investing activities | (11,451) | (12,649) | (19,009) | (20,364) |
| Cash flows from (used in) financing activities | | | | |
| Repurchase of notes and repayment of debt | | (10,763) | (23,079) | (10,763) |
| Dividend payments | (7,435) | | (14,853) | |
| Proceeds from (repayment of) revolving credit facilities, net | | 8,570 | | 9,523 |
| Payment of interest rate derivative liability | (5,852) | (7,015) | (5,852) | (7,015) |
| Other | (517) | (403) | (1,003) | (621) |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Net cash from (used in) financing activities | | (13,804) | | (9,611) | | (44,787) | | (8,876) |
| | | | | | | | | |
| Effect of exchange rate changes on cash and cash equivalents | | (3,240) | | 2,850 | | 2,075 | | (3,344) |
| | | | | | | | | |
| Net increase (decrease) in cash and cash equivalents | | (17,218) | | (8,976) | | 13,022 | | 37,695 |
| Cash and cash equivalents, beginning of period | | 129,869 | | 99,843 | | 99,629 | | 53,172 |
| Cash and cash equivalents, end of period | $ | 112,651 | $ | 90,867 | $ | 112,651 | $ | 90,867 |
| | | | | | | | | |
| Supplemental cash flow disclosure | | | | | | | | |
| Cash paid for interest | $ | 24,036 | $ | 25,779 | $ | 24,635 | $ | 25,905 |
| Cash paid for income taxes | $ | 4,681 | $ | 402 | $ | 9,311 | $ | 815 |

*The accompanying notes are an integral part of these interim consolidated financial statements.*

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 1. The Company and Summary of Significant Accounting Policies**

***Nature of Operations and Basis of Presentation***

The interim consolidated financial statements contained herein include the accounts of Mercer International Inc. ( Mercer Inc. ) and all of its subsidiaries (collectively the Company ). The Company s shares of common stock are quoted and listed for trading on both the NASDAQ Global Market and the Toronto Stock Exchange.

The interim consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the United States Securities and Exchange Commission (the SEC ). The year-end Consolidated Balance Sheet data was derived from audited financial statements. The footnote disclosure included herein has been prepared in accordance with accounting principles generally accepted for interim financial statements in the United States ( GAAP ). The interim consolidated financial statements should be read together with the audited consolidated financial statements and accompanying notes included in the Company s latest annual report on Form 10-K for the fiscal year ended December 31, 2015. In the opinion of the Company, the unaudited interim consolidated financial statements contained herein contain all adjustments necessary for a fair statement of the results of the interim periods included. The results for the periods included herein may not be indicative of the results for the entire year.

The Company has three pulp mills that are aggregated into one reportable business segment, market pulp. Accordingly, the results presented are those of the reportable business segment.

In these interim consolidated financial statements, unless otherwise indicated, all amounts are expressed in United States dollars ( U.S. dollars or $ ). The symbol refers to euros and the symbol C$ refers to Canadian dollars.

***Use of Estimates***

Preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant management judgment is required in determining the accounting for, among other things, pension and other post-retirement benefit obligations, deferred income taxes (valuation allowance and permanent reinvestment), depreciation and amortization, future cash flows associated with impairment testing for long-lived assets, legal liabilities and contingencies. Actual results could differ materially from these estimates, and changes in these estimates are recorded when known.

***New Accounting Pronouncements***

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update 2014-9, Revenue Recognition Revenue from Contracts with Customers ( ASU 2014-9 ) that requires companies to recognize revenue when a customer obtains control rather than when companies have transferred substantially all risks and rewards of a good or service. This update is effective for annual reporting periods beginning on or after December 15, 2017 and interim periods therein and requires expanded disclosures. The Company is currently assessing the impact, if any, the adoption of ASU 2014-9 will have on its consolidated financial statements.

In July 2015, the Financial Accounting Standards Board issued Accounting Standards Update 2015-11, Simplifying the Measurement of Inventory (  ASU 2015-11  ) which requires that inventory within the scope of this update, including inventory stated at average cost, be measured at the lower of cost and net realizable value. This update is effective for financial statements issued for fiscal years beginning after December 15, 2016, with early adoption permitted as of the beginning of an interim or annual reporting period. The adoption of this accounting guidance will not materially impact the Company  s financial position.

In February 2016, the Financial Accounting Standards Board issued Accounting Standards Update 2016-2, Leases (  ASU 2016-2  ) which requires lessees to recognize virtually all of their leases on the balance sheet, by recording a right-of-use asset and liability. This update is effective for financial statements issued for fiscal years beginning after December 15, 2018, with early adoption permitted as of the beginning of an interim or annual reporting period. The Company is currently assessing the impact the adoption of ASU 2016-2 will have on its consolidated financial statements.

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 1. The Company and Summary of Significant Accounting Policies (continued)**

In March 2016, the Financial Accounting Standards Board issued Accounting Standards Update 2016-9, Improvements to Employee Share-Based Payment Accounting ( ASU 2016-9 ) which simplifies several aspects of accounting for share-based payment transactions including income tax consequences, classification of awards as either equity or liabilities, classification on the statement of cash flows and accounting for forfeitures. This update is effective for financial statements issued for fiscal years beginning after December 15, 2016. The Company is currently assessing the impact, if any, the adoption of ASU 2016-9 will have on its consolidated financial statements.

**Note 2. Inventories**

| | | June 30, 2016 | | December 31, 2015 |
|---|---|---|---|---|
| Raw materials | $ | 50,796 | $ | 57,592 |
| Finished goods | | 33,859 | | 36,829 |
| Spare parts and other | | 50,192 | | 46,580 |
| | $ | 134,847 | $ | 141,001 |

**Note 3. Accounts Payable and Other**

| | | June 30, 2016 | | December 31, 2015 |
|---|---|---|---|---|
| Trade payables | $ | 26,293 | $ | 20,637 |
| Accrued expenses | | 51,321 | | 55,648 |
| Accrued interest payable | | 4,040 | | 4,050 |
| Interest rate derivative liability, current portion (Note 10) | | 8,882 | | 10,380 |
| Dividend payable (Note 7) | | 7,440 | | 7,418 |
| Other | | 5,519 | | 5,317 |
| | $ | 103,495 | $ | 103,450 |

**Note 4. Debt**

| | | June 30, 2016 | | December 31, 2015 |
|---|---|---|---|---|
| 2019 Senior Notes, unsecured, $227,000 face value (a) | $ | 223,586 | $ | 245,689 |
| 2022 Senior Notes, unsecured, $400,000 face value (a) | | 392,906 | | 392,354 |
| Revolving credit facilities | | | | |
| 75.0 million (b) | | | | |
| C$40.0 million (c) | | | | |
| 25.0 million (d) | | | | |
| 5.0 million (e) | | | | |
| | $ | 616,492 | $ | 638,043 |

As at June 30, 2016, the maturities of the principal portion of debt are as follows:

| | | |
|---|---|---|
| 2016 | $ | |
| 2017 | | |
| 2018 | | |
| 2019 | | 227,000 |
| 2020 | | |
| Thereafter | | 400,000 |
| | $ | 627,000 |

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 4. Debt (continued)**

Certain of the Company s debt instruments were issued under agreements which, among other things, may limit its ability and the ability of its subsidiaries to make certain payments, including dividends. These limitations are subject to specific exceptions. As at June 30, 2016, the Company is in compliance with the terms of its debt agreements.

(a) On November 26, 2014, the Company issued $650,000 of senior notes consisting of $250,000 in aggregate principal amount of 7.00% senior notes which mature on December 1, 2019 ( 2019 Senior Notes ) and $400,000 in aggregate principal amount of 7.75% senior notes which mature on December 1, 2022 ( 2022 Senior Notes and collectively with the 2019 Senior Notes, the Senior Notes ). The Senior Notes were issued at a price of 100% of their principal amount. Upon their issuance the Senior Notes were recorded at $635,949 which included debt issuance costs of $14,051. These costs were proportionally allocated to the 2019 Senior Notes and the 2022 Senior Notes.

The Senior Notes are general unsecured senior obligations of the Company. They rank equal in right of payment with all existing and future unsecured senior indebtedness of the Company and are senior in right of payment to any current or future subordinated indebtedness of the Company. The Senior Notes are effectively junior in right of payment to all existing and future secured indebtedness, to the extent of the assets securing such indebtedness, and all indebtedness and liabilities of the Company s subsidiaries.

The Company may redeem all or a part of the Senior Notes, upon not less than 30 days or more than 60 days notice, at the redemption prices (expressed as percentages of principal amount) discussed below, plus accrued and unpaid interest to (but not including) the applicable redemption date. The 2019 Senior Notes redemption prices are equal to 103.50% for the twelve month period beginning on December 1, 2016, 101.75% for the twelve month period beginning on December 1, 2017, and 100.00% beginning on December 1, 2018 and at any time thereafter. The 2022 Senior Notes redemption prices are equal to 105.813% for the twelve month period beginning on December 1, 2017, 103.875% for the twelve month period beginning on December 1, 2018, 101.938% for the twelve month period beginning on December 1, 2019, and 100.00% beginning on December 1, 2020 and at any time thereafter.

In March 2016, the Company purchased $23,000 in aggregate principal amount of its 2019 Senior Notes. In connection with this purchase the Company recorded a loss on extinguishment of debt of $454 in other income (expenses) in the Interim Consolidated Statement of Operations which included the write-off of unamortized debt issuance costs.

(b)

A 75.0 million revolving credit facility at the Stendal mill that matures in October 2019. Borrowings under the facility are collateralized by the mill s inventory and accounts receivable and bear interest at Euribor plus 3.50%. As at June 30, 2016, approximately 75.0 million ($82,755) was available.

(c) A C$40.0 million revolving credit facility at the Celgar mill that matures in May 2019. Borrowings under the facility are collateralized by the mill s inventory and accounts receivable and are restricted by a borrowing base calculated on the mill s inventory and accounts receivable. Canadian dollar denominated amounts bear interest at bankers acceptance plus 1.50% or Canadian prime. U.S. dollar denominated amounts bear interest at LIBOR plus 1.50% or U.S. base. As at June 30, 2016, approximately C$1.7 million ($1,308) was supporting letters of credit and approximately C$38.3 million ($29,440) was available.

(d) A 25.0 million revolving credit facility at the Rosenthal mill that matures in October 2019. Borrowings under the facility are collateralized by the mill s inventory and accounts receivable and bear interest at Euribor plus 2.95%. As at June 30, 2016, approximately 3.1 million ($3,378) of this facility was supporting bank guarantees leaving approximately 21.9 million ($24,207) available.

(e) A 5.0 million revolving credit facility at the Rosenthal mill that matures in December 2018. Borrowings under this facility bear interest at the rate of the three-month Euribor plus 2.50% and are secured by certain land at the Rosenthal mill. As at June 30, 2016, approximately 3.8 million ($4,174) of this facility was supporting bank guarantees leaving approximately 1.2 million ($1,343) available.

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 5. Pension and Other Post-Retirement Benefit Obligations**

***Defined Benefit Plans***

Included in pension and other post-retirement benefit obligations are amounts related to the Company s Celgar and Rosenthal mills. The largest component of these obligations is with respect to the Celgar mill which maintains a defined benefit pension plan and other post-retirement benefit plans for certain employees (the Celgar Defined Benefit Plans ).

Pension benefits are based on employees earnings and years of service. The Celgar Defined Benefit Plans are funded by contributions from the Company based on actuarial estimates and statutory requirements.

The components of the net periodic benefit costs relating to the Celgar Defined Benefit Plans for the three and six month periods ended June 30, 2016 and 2015 were as follows:

| | Three Months Ended June 30, | | | |
|---|---|---|---|---|
| | 2016 | | 2015 | |
| | Pension | Other Post-Retirement Benefits | Pension | Other Post-Retirement Benefits |
| Service cost | $ 23 | $ 124 | $ 32 | $ 208 |
| Interest cost | 236 | 220 | 276 | 172 |
| Expected return on plan assets | (494) | | (534) | |
| Amortization of unrecognized items | 333 | (44) | 229 | 2 |
| Net periodic benefit cost | $ 98 | $ 300 | $ 3 | $ 382 |

| | Six Months Ended June 30, | | | |
|---|---|---|---|---|
| | 2016 | | 2015 | |
| | Pension | Other Post-Retirement Benefits | Pension | Other Post-Retirement Benefits |
| Service cost | $ 45 | $ 241 | $ 63 | $ 413 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Interest cost | | 497 | | 471 | | 724 | | 498 |
| Expected return on plan assets | | (959) | | | | (1,063) | | |
| Amortization of unrecognized items | | 667 | | (88) | | 455 | | 4 |
| Net periodic benefit cost | $ | 250 | $ | 624 | $ | 179 | $ | 915 |

***Defined Contribution Plan***

Effective December 31, 2008, the Celgar Defined Benefit Plans were closed to new members. In addition, the defined benefit service accrual ceased on December 31, 2008, and members began to receive pension benefits, at a fixed contractual rate, under a new defined contribution plan effective January 1, 2009. During the three and six month periods ended June 30, 2016, the Company made contributions of $146 and $309, respectively (2015 $179 and $348), to this plan.

***Multiemployer Plan***

The Company participates in a multiemployer plan for the hourly-paid employees at the Celgar mill. The contributions to the plan are determined based on a percentage of pensionable earnings pursuant to a collective bargaining agreement. The Company has no current or future contribution obligations in excess of the contractual contributions. Contributions during the three and six month periods ended June 30, 2016 totaled $407 and $783, respectively (2015 $399 and $850).

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 6. Income Taxes**

The income tax provision attributable to income before provision for income taxes differs from the amounts computed by applying the U.S. federal statutory income tax rate of 35% for the three and six month periods ended June 30, 2016 and 2015 as a result of the following:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | **2016** | **2015** | **2016** | **2015** |
| U.S. Federal statutory rate | 35% | 35% | 35% | 35% |
| U.S. Federal statutory rate on income before income taxes | $ (1,271) | $ (7,819) | $ (6,510) | $ (15,833) |
| Tax differential on foreign income | 149 | 1,899 | 1,634 | 3,925 |
| Effect of foreign earnings | | (5,290) | (3,500) | (5,290) |
| Valuation allowance | (9,942) | (1,440) | (9,742) | (6,401) |
| Tax benefit of partnership structure | 1,364 | 1,303 | 2,563 | 2,592 |
| Non-taxable foreign subsidies | 545 | 566 | 1,118 | 1,145 |
| True-up of prior year taxes | 558 | 4,610 | (60) | 4,603 |
| Other | 724 | 244 | 425 | 67 |
| | $ (7,873) | $ (5,927) | $ (14,072) | $ (15,192) |
| Comprised of: | | | | |
| Current | $ (3,372) | $ (3,149) | $ (5,125) | $ (6,501) |
| Deferred | (4,501) | (2,778) | (8,947) | (8,691) |
| | $ (7,873) | $ (5,927) | $ (14,072) | $ (15,192) |

For the three and six month periods ended June 30, 2016, the Company recorded an increase in its valuation allowance of $9,942 and $9,742 respectively (2015 $1,440 and $6,401), related to its U.S. and Canadian entities where a full valuation allowance was recognized against net deferred income tax assets.

**Note 7. Shareholders Equity**

***Dividends***

During the six month period ended June 30, 2016, the Company s Board of Directors declared the following quarterly dividends:

| Date Declared | Dividend Per Common Share | | Amount | |
|---|---|---|---|---|
| February 11, 2016 | $ | 0.115 | $ | 7,435 |
| April 28, 2016 | $ | 0.115 | $ | 7,440 |
| | $ | 0.230 | $ | 14,875 |

Dividends are paid in the quarter subsequent to the quarter in which they were declared.

In July 2016, the Company s Board of Directors declared a quarterly dividend of $0.115 per common share. Payment of the dividend will be made on October 4, 2016 to all shareholders of record on September 26, 2016. Future dividends are subject to approval by the Board of Directors and may be adjusted as business and industry conditions warrant.

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 7. Shareholders Equity (continued)**

***Stock Based Compensation***

In June 2010, the Company adopted a stock incentive plan (the 2010 Plan ) which provides for options, restricted stock rights, restricted shares, performance shares, performance share units ( PSUs ) and stock appreciation rights to be awarded to employees, consultants and non-employee directors. During the six months ended June 30, 2016, there were no issued and outstanding stock options, restricted stock rights, performance shares or stock appreciation rights. As at June 30, 2016, after factoring in all allocated shares, there remain approximately 1,013,112 common shares available for grant.

*PSUs*

PSUs comprise rights to receive common shares at a future date that are contingent on the Company and the grantee achieving certain performance objectives. The performance objective period is generally three years.

For the three and six month periods ended June 30, 2016, the Company recognized an expense of $649 and $1,386, respectively, related to PSUs (2015 $596 and $1,097).

The following table summarizes PSU activity during the period:

| | **Number of PSUs** |
|---|---|
| Outstanding at January 1, 2016 | 1,255,919 |
| Granted | 997,863 |
| Vested and issued | (154,242) |
| Outstanding at June 30, 2016 | 2,099,540 |

*Restricted Shares*

Restricted shares generally vest at the end of one year; however, 200,000 restricted shares granted during the year ended December 31, 2011 vested in equal amounts over a five-year period commencing in 2012.

For the three and six month periods ended June 30, 2016, the Company recognized an expense of $115 and $269, respectively, related to restricted shares (2015    $132 and $261). As at June 30, 2016, the total remaining unrecognized compensation cost related to restricted shares amounted to approximately $333 which will be amortized over the remaining vesting periods.

The following table summarizes restricted share activity during the period:

| | **Number of Restricted Shares** |
|---|---|
| Outstanding at January 1, 2016 | 78,000 |
| Granted | 38,000 |
| Vested and issued | (78,000) |
| Outstanding at June 30, 2016 | 38,000 |

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 7. Shareholders Equity (continued)**

***Retained Earnings***

The following table summarizes the changes in retained earnings during the period:

| | Six Months Ended June 30, 2016 |
|---|---|
| Retained earnings, January 1, 2016 | $ 160,880 |
| Net income | 4,528 |
| Cash dividends declared ($0.23 per common share) | (14,875) |
| Retained earnings, June 30, 2016 | $ 150,533 |

**Note 8. Net Income (Loss) Per Common Share**

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Net income (loss) | | | | |
| Basic and diluted | $ (4,241) | $ 16,412 | $ 4,528 | $ 30,046 |
| | | | | |
| Net income (loss) per common share | | | | |
| Basic | $ (0.07) | $ 0.25 | $ 0.07 | $ 0.47 |
| Diluted | $ (0.07) | $ 0.25 | $ 0.07 | $ 0.46 |
| | | | | |
| Weighted average number of common shares outstanding: | | | | |
| Basic[(1)] | 64,628,160 | 64,395,918 | 64,606,572 | 64,336,515 |
| Effect of dilutive shares: | | | | |
| PSUs | | 329,943 | 348,339 | 335,729 |
| Restricted shares | | 55,111 | 28,862 | 71,736 |

| | | | | |
|---|---|---|---|---|
| Diluted | 64,628,160 | 64,780,972 | 64,983,773 | 64,743,980 |

(1) For the three and six month periods ended June 30, 2016, the basic weighted average number of common shares outstanding excludes 38,000 restricted shares which have been issued, but have not vested as at June 30, 2016 (2015 78,000 restricted shares).

The calculation of diluted net income (loss) per common share does not assume the exercise of any instruments that would have an anti-dilutive effect on net income (loss) per common share. The following table summarizes the instruments excluded from the calculation of net income (loss) per common share because they were anti-dilutive:

| | **Three Months Ended June 30,** | | **Six Months Ended June 30,** | |
|---|---|---|---|---|
| | **2016** | **2015** | **2016** | **2015** |
| PSUs | 2,099,540 | | | |
| Restricted shares | 38,000 | | | |

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 9. Accumulated Other Comprehensive Loss**

The components of accumulated other comprehensive loss are as follows:

| | Foreign Currency Translation Adjustment | Unrecognized Losses and Prior Service Costs Related to Defined Benefit Plan | Unrealized Gains (Losses) on Marketable Securities | Total |
|---|---|---|---|---|
| Balance December 31, 2015 | $ (156,223) | $ (15,338) | $ (13) | $ (171,574) |
| Other comprehensive income (loss) before reclassifications | 25,355 | | 2 | 25,357 |
| Amounts reclassified from accumulated other comprehensive income (loss) | | 579 | | 579 |
| Other comprehensive income (loss), net of taxes | 25,355 | 579 | 2 | 25,936 |
| Balance June 30, 2016 | $ (130,868) | $ (14,759) | $ (11) | $ (145,638) |

**Note 10. Derivative Transactions**

The Company is exposed to certain market risks relating to its ongoing business. The Company seeks to manage these risks through internal risk management policies as well as, from time to time, the use of derivatives. The derivatives are measured at fair value with changes in fair value immediately recognized in other income (expenses) in the Interim Consolidated Statement of Operations.

***Interest Rate Swaps***

During 2002, the Company entered into certain variable-to-fixed interest rate swaps in connection with the Stendal mill with respect to an aggregate maximum amount of approximately   612.6 million of the principal amount of the indebtedness under the Stendal mill  s senior project finance facility, which was settled in November 2014. Under the remaining interest rate swaps, the Company pays a fixed rate and receives a floating rate with the derivative payments being calculated on a notional amount. As at June 30, 2016, the contract has a fair value of 10.7 million ($11,780; 2015 $16,913) of which 8.1 million ($8,882; 2015 $10,380) is classified as current within accounts payable and other and 2.6 million ($2,898; 2015 $6,533) is classified as a long-term liability in the Interim Consolidated Balance Sheet. The contract has an aggregate notional amount of 161.0 million, a fixed interest rate of 5.28% and matures in October 2017.

The Company has pledged as collateral cash in the amount of 67% of the fair value of the interest rate swaps up to 8.5 million to the derivative counterparty. The calculation to determine the collateral is performed semi-annually, with the final calculation in October 2017. As at June 30, 2016, the collateral was 7.1 million ($7,834; 2015 $9,230). This cash has been classified as restricted cash in the Interim Consolidated Balance Sheet.

During the three and six month periods ended June 30, 2016 the Company recorded a loss on the interest rate swaps of $55 and $265, respectively (2015 gain of $167 and loss of $357), in other income (expenses) in the Interim Statement of Operations.

The counterparty to the interest rate swaps is a bank that is a member of a banking syndicate that holds the Stendal 75.0 million revolving credit facility and the Company does not anticipate non-performance by the bank.

**MERCER INTERNATIONAL INC.**

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**(In thousands of U.S. dollars, except share and per share data)**

**Note 11. Fair Value Measurement and Disclosure**

Due to their short-term maturity, the carrying amounts of cash and cash equivalents, restricted cash, accounts receivable and accounts payable and other approximates their fair value.

The fair value of the interest rate derivative liability classified as Level 2 is determined using a discounted cash flow model that uses as its basis readily observable market inputs, such as forward interest rates and yield curves observable at specified intervals. The observable inputs reflect market data obtained from independent sources, including the Euribor rate provided by the counterparty to the interest rate derivative.

The fair value of the Senior Notes debt classified as Level 2 is determined using quoted prices in a dealer market, or using recent market transactions.

The following tables present a summary of the Company s outstanding financial instruments and their estimated fair values under the fair value hierarchy:

| | Fair value measurements as at June 30, 2016 using: | | | |
|---|---|---|---|---|
| **Description** | **Level 1** | **Level 2** | **Level 3** | **Total** |
| Interest rate derivative liability | $ | $ 11,780 | $ | $ 11,780 |
| Senior Notes debt | | 629,270 | | 629,270 |
| | $ | $ 641,050 | $ | $ 641,050 |

| | Fair value measurements as at December 31, 2015 using: | | | |
|---|---|---|---|---|
| **Description** | **Level 1** | **Level 2** | **Level 3** | **Total** |
| Interest rate derivative liability | $ | $ 16,913 | $ | $ 16,913 |
| Senior Notes debt | | 654,625 | | 654,625 |
| | $ | $ 671,538 | $ | $ 671,538 |

**Note 12. Commitments and Contingencies**

(a) The Company is involved in legal actions and claims arising in the ordinary course of business. While the outcome of any legal actions and claims cannot be predicted with certainty, it is the opinion of management that the outcome of any such claims which are pending or threatened, either individually or on a combined basis, will not have a material adverse effect on the consolidated financial condition, results of operations or liquidity of the Company.

(b) In 2012, as a result of a regular tax field audit for the Stendal mill, German public authorities commenced a preliminary investigation into past managers of the mill relating to whether certain settlement amounts received by the Stendal mill in 2007, 2010 and 2011 from the main contractor under the contract for the construction of the Stendal mill should have reduced the assessment base for the original investment subsidies granted to the mill by German public authorities. In March 2016, the German public authorities closed its investigation of the past managers of the mill, with no action taken against them or the Company.

(c) The Company is subject to regulations that require the handling and disposal of asbestos in a prescribed manner if a property undergoes a major renovation or demolition. Otherwise, the Company is not required to remove asbestos from its facilities. Generally asbestos is found on steam and condensate piping systems as well as certain cladding on buildings and in building insulation throughout older facilities. The Company s obligation for the proper removal and disposal of asbestos products from the Company s mills is a conditional asset retirement obligation. As a result of the longevity of the Company s mills, due in part to the maintenance procedures and the fact that the Company does not have plans for major changes that require the removal of asbestos, the timing of the asbestos removal is indeterminate. As a result, the Company is currently unable to reasonably estimate the fair value of its asbestos removal and disposal obligation. The Company will recognize a liability in the period in which sufficient information is available to reasonably estimate its fair value.

## NON-GAAP FINANCIAL MEASURES

This quarterly report on Form 10-Q contains non-GAAP financial measures , that is, financial measures that either exclude or include amounts that are not excluded or included in the most directly comparable measure calculated and presented in accordance with the generally accepted accounting principles in the United States, referred to as GAAP . Specifically, we make use of the non-GAAP measure Operating EBITDA .

Operating EBITDA is defined as operating income (loss) plus depreciation and amortization and non-recurring capital asset impairment charges. We use Operating EBITDA as a benchmark measurement of our own operating results and as a benchmark relative to our competitors. We consider it to be a meaningful supplement to operating income as a performance measure primarily because depreciation expense and non-recurring capital asset impairment charges are not actual cash costs, and depreciation expense varies widely from company to company in a manner that we consider largely independent of the underlying cost efficiency of our operating facilities. In addition, we believe Operating EBITDA is commonly used by securities analysts, investors and other interested parties to evaluate our financial performance.

Operating EBITDA does not reflect the impact of a number of items that affect our net income (loss), including financing costs and the effect of derivative instruments. Operating EBITDA is not a measure of financial performance under GAAP, and should not be considered as an alternative to net income (loss) or income (loss) from operations as a measure of performance, or as an alternative to net cash from operating activities as a measure of liquidity. Operating EBITDA is an internal measure and therefore may not be comparable to other companies.

Operating EBITDA has significant limitations as an analytical tool, and should not be considered in isolation, or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are that Operating EBITDA does not reflect: (i) our cash expenditures, or future requirements, for capital expenditures or contractual commitments; (ii) changes in, or cash requirements for, working capital needs; (iii) the significant interest expense, or the cash requirements necessary to service interest or principal payments, on our outstanding debt; (iv) the impact of realized or marked to market changes in our derivative positions, which can be substantial; and (v) the impact of impairment charges against our investments or assets. Because of these limitations, Operating EBITDA should only be considered as a supplemental performance measure and should not be considered as a measure of liquidity or cash available to us to invest in the growth of our business. Because all companies do not calculate Operating EBITDA in the same manner, Operating EBITDA as calculated by us may differ from Operating EBITDA or EBITDA as calculated by other companies. We compensate for these limitations by using Operating EBITDA as a supplemental measure of our performance and by relying primarily on our GAAP financial statements.

## ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In this document: (i) unless the context otherwise requires, references to we , our , us , the Company or Mercer Mercer International Inc. and its subsidiaries; (ii) references to Mercer Inc. mean the Company excluding its subsidiaries; (iii) information is provided as of June 30, 2016, unless otherwise stated; (iv) our reporting currency is dollars and references to mean euros and C$ mean Canadian dollars; (v) ADMTs refers to air-dried metric tonne and (vi) MW refers to megawatts and MWh refers to megawatt hours.

**Results of Operations**

***General***

We operate in the pulp business and our operations are located in Germany and Western Canada. Our mills have a current combined annual production capacity of approximately 1.5 million ADMTs of northern bleached softwood kraft pulp, referred to as NBSK pulp , and 305 MW of electrical generation.

The following discussion and analysis of our results of operations and financial condition for the three and six months ended June 30, 2016 should be read in conjunction with our interim consolidated financial statements and related notes included in this quarterly report, as well as our most recent annual report on Form 10-K for the fiscal year ended December 31, 2015 filed with the Securities and Exchange Commission, referred to as the SEC .

***Current Market Environment***

In the second quarter of 2016, pulp prices in Europe, China and North America increased modestly compared to the prior quarter of 2016 as a result of steady demand, relatively low supplier inventories and the impact of spring maintenance downtime. This resulted in our average pulp sales realizations being approximately 2% higher in the second quarter of 2016 compared to the prior quarter of 2016. At the end of the current quarter, list prices in Europe, China and North America were approximately $810, $630 and $1,000 per ADMT, respectively.

Currently, the NBSK pulp market is balanced with world producer inventories at about 28 days supply.

Looking forward, we currently expect steady pulp demand and pricing in the third quarter of 2016 in Europe and China, but with the possibility of some temporary weakness in spot pricing in China during the typically slow summer period.

Our current 2016 annual maintenance downtime schedule for our mills is:

| 2016 Quarter | Celgar | Rosenthal | Stendal |
|---|---|---|---|
| | (number of days) | | |
| Third | - | 12 | - |
| Fourth | - | - | 12 |

***Summary Financial Highlights***

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands, other than per share amounts) | | | |
| Pulp revenues | $ 198,055 | $ 246,126 | $ 428,684 | $ 480,783 |
| Energy and chemical revenues | $ 20,090 | $ 20,810 | $ 43,304 | $ 43,700 |
| Operating income | $ 16,777 | $ 33,549 | $ 44,877 | $ 77,480 |
| Operating EBITDA[(1)] | $ 34,739 | $ 50,032 | $ 80,058 | $ 111,350 |
| Foreign exchange (loss) gain on intercompany debt | $ (272) | $ 2,198 | $ 283 | $ (4,412) |
| Income tax provision | $ (7,873) | $ (5,927) | $ (14,072) | $ (15,192) |
| Net (loss) income | $ (4,241) | $ 16,412 | $ 4,528 | $ 30,046 |
| Net (loss) income per common share | | | | |
| Basic | $ (0.07) | $ 0.25 | $ 0.07 | $ 0.47 |
| Diluted | $ (0.07) | $ 0.25 | $ 0.07 | $ 0.46 |
| Common shares outstanding at period end | 64,694 | 64,502 | 64,694 | 64,502 |

(1) The following table provides a reconciliation of net income (loss) to operating income and Operating EBITDA for the periods indicated:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| | (in thousands) | | | |
| Net (loss) income | $ (4,241) | $ 16,412 | $ 4,528 | $ 30,046 |
| Income tax provision | 7,873 | 5,927 | 14,072 | 15,192 |
| Interest expense | 12,736 | 13,476 | 25,927 | 27,360 |
| Foreign exchange loss (gain) on intercompany debt | 272 | (2,198) | (283) | 4,412 |
| Other expenses (income) | 137 | (68) | 633 | 470 |
| Operating income | 16,777 | 33,549 | 44,877 | 77,480 |
| Add: Depreciation and amortization | 17,962 | 16,483 | 35,181 | 33,870 |
| Operating EBITDA | $ 34,739 | $ 50,032 | $ 80,058 | $ 111,350 |

***Selected Production, Sales and Other Data***

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Pulp production ( 000 ADMTs) | 338.3 | 358.9 | 716.3 | 721.5 |

| | | | | |
|---|---|---|---|---|
| Annual maintenance downtime (  000 ADMTs) | 29.6 | 20.6 | 29.6 | 39.8 |
| Annual maintenance downtime (days) | 21 | 11 | 21 | 25 |
| Pulp sales (  000 ADMTs) | 330.3 | 371.4 | 723.8 | 721.0 |
| Average NBSK pulp list prices in Europe ($/ADMT)[1] | 798 | 855 | 795 | 871 |
| Average NBSK pulp list prices in China ($/ADMT)[1] | 617 | 670 | 603 | 667 |
| Average NBSK pulp list prices in North America ($/ADMT)[1] | 980 | 980 | 962 | 988 |
| Average pulp sales realizations ($/ADMT)[2] | 592 | 657 | 586 | 661 |
| Energy production (  000 MWh) | 431.5 | 450.3 | 907.1 | 905.4 |
| Energy sales (  000 MWh) | 190.3 | 196.5 | 397.6 | 395.7 |
| Average energy sales realizations ($/MWh) | 86 | 89 | 90 | 92 |
| | | | | |
| **Average Spot Currency Exchange Rates** | | | | |
| $/ [3] | 1.1295 | 1.1069 | 1.1167 | 1.1155 |
| $ / C$[3] | 0.7762 | 0.8134 | 0.7535 | 0.8097 |

(1) Source: RISI pricing report.
(2) Sales realizations after discounts. Incorporates the effect of pulp price variations occurring between the order and shipment dates.
(3) Average Federal Reserve Bank of New York Noon Buying Rates over the reporting period.

***Three Months Ended June 30, 2016 Compared to Three Months Ended June 30, 2015***

Total revenues for the three months ended June 30, 2016 decreased by approximately 18% to $218.1 million from $266.9 million in the same quarter of 2015, primarily due to lower pulp revenues.

Pulp revenues in the second quarter of 2016 decreased by approximately 20% to $198.1 million from $246.1 million in the same quarter of 2015, due to lower sales volumes resulting from lower production and lower pulp sales realizations.

In the second quarter of 2016, our German mills operated very well, but our Celgar mill had a number of challenges. Its annual maintenance downtime, initially scheduled for 12 days, was extended to 18 days (approximately 24,500 ADMTs) in order to effect additional work that was identified. After completion of such maintenance work, the mill restart was adversely affected by several unexpected factors, including mechanical failures and a disruption to the mill s power supply. These factors collectively resulted in the mill not returning to normalized production for a period of approximately ten days. The aggregate effect of the maintenance downtime and slow restart of the mill was a reduction of approximately 37,900 ADMTs of pulp production and 15,000 MWh of surplus energy.

The maintenance downtime and slow restart of the Celgar mill also disrupted our pulp sales, as approximately 10,000 ADMTs that were scheduled to be shipped and sold in June were delayed to the third quarter of 2016.

Energy and chemical revenues decreased by approximately 3% to $20.1 million in the second quarter of 2016 from $20.8 million in the same quarter of 2015, primarily due to lower energy generation and sales volumes at our Celgar mill.

Pulp production decreased by approximately 6% to 338,265 ADMTs in the current quarter from 358,861 ADMTs in the same quarter of 2015. In the second quarter of 2016, we had an aggregate of 21 days (approximately 29,600 ADMTs) of annual maintenance downtime, of which 18 days was at our Celgar mill and three days (approximately 5,100 ADMTs) was at our Stendal mill. In the comparative quarter of 2015, we had 11 days (approximately 20,600 ADMTs) of annual maintenance downtime at our Stendal mill.

We estimate that annual maintenance downtime in the current quarter adversely impacted our Operating EBITDA by approximately $20.6 million, comprised of approximately $15.2 million in direct out-of-pocket expenses and the balance in reduced production. Many of our competitors that report their financial results using International Financial Reporting Standards ( IFRS ) capitalize their direct costs of maintenance downtime.

Pulp sales volumes decreased by approximately 11% to 330,318 ADMTs in the current quarter from 371,350 ADMTs in the same quarter of 2015, primarily due to lower production at our Celgar mill.

In the current quarter of 2016, list prices for NBSK pulp in Europe and China declined from the same quarter of 2015, largely as a result of the strong dollar and weakening hardwood prices impacting NBSK pulp prices. Average list prices for NBSK pulp in Europe were approximately $798 per ADMT in the second quarter of 2016, compared to approximately $855 per ADMT in the same quarter of 2015. Average list prices for NBSK pulp in China and North America were approximately $617 per ADMT and $980 per ADMT, respectively, in the second quarter of 2016, compared to approximately $670 per ADMT and $980 per ADMT, respectively, in the same quarter of 2015.

Average pulp sales realizations decreased by approximately 10% to $592 per ADMT in the second quarter of 2016 from approximately $657 per ADMT in the same quarter last year, primarily due to lower list prices.

Near the end of the current quarter, the dollar strengthened versus the euro and as at June 30, 2016 was approximately 3% higher, compared to March 31, 2016. This resulted in a positive impact on our dollar-denominated cash balances and receivables of $3.8 million.

Costs and expenses in the current quarter decreased by approximately 14% to $201.4 million from $233.4 million in the second quarter of 2015, primarily due to lower sales volumes, the reversal of an accrual for wastewater fees at our Rosenthal mill of $7.2 million and lower fiber prices, partially offset by higher annual maintenance costs. During the current quarter, regulatory authorities accepted that a capital project at the Rosenthal mill reduced wastewater discharges and, as a result, we reversed its accrual for wastewater fees that would otherwise have been payable.

In the second quarter of 2016, operating depreciation and amortization was $17.9 million, compared to $16.4 million in the same quarter of 2015.

Selling, general and administrative expenses decreased to $10.3 million in the second quarter of 2016 from $11.7 million in the same quarter of 2015.

Transportation costs decreased by approximately 25% to $15.0 million in the current quarter from $20.1 million in the same quarter of 2015 primarily due to lower shipments from our Celgar mill resulting from its maintenance downtime and slow restart.

On average, in the current quarter overall fiber prices decreased by approximately 3% from the same quarter of 2015, primarily as a result of a balanced wood market and strong sawmilling activity in both Germany and in the Celgar mill s fiber basket. In the current quarter, in euro terms, average fiber prices in Germany were approximately 9% lower than the comparative quarter. In the current quarter, in Canadian dollar terms, average fiber prices for our Celgar mill were marginally lower than the comparative quarter.

In the second quarter of 2016, our operating income decreased by approximately 50% to $16.8 million from $33.5 million in the same quarter of 2015, primarily due to 10% lower pulp sales realizations, the net impact of lower sales volumes and higher annual maintenance costs, partially offset by the reversal of a $7.2 million wastewater fee accrual at our Rosenthal mill, lower fiber prices and the strengthening of the dollar versus the euro near the end of the quarter.

Interest expense in the current quarter decreased to $12.7 million from $13.5 million in the same quarter of 2015, primarily as a result of lower indebtedness.

As a result of the strengthening of the dollar versus the euro at the end of the second quarter of 2016, we recorded a non-cash loss on the foreign exchange translation of certain intercompany debt between Mercer Inc. and its wholly owned subsidiaries, which increased our net loss by $0.3 million.

During the second quarter of 2016, income tax expense increased to $7.9 million from $5.9 million in the same quarter of 2015 due to higher taxable income for our German mills.

For the second quarter of 2016, we had a net loss of $4.2 million, or $0.07 per basic and diluted share compared to net income of $16.4 million, or $0.25 per basic and diluted share, in the same quarter of 2015.

In the second quarter of 2016, Operating EBITDA decreased by approximately 31% to $34.7 million from $50.0 million in the same quarter of 2015, primarily as a result of lower pulp sales realizations, the net impact of lower sales volumes and higher annual maintenance costs, partially offset by the reversal of a wastewater fee accrual at our Rosenthal mill, lower fiber prices and the strengthening of the dollar versus the euro near the end of the quarter.

***Six Months Ended June 30, 2016 Compared to Six Months Ended June 30, 2015***

Total revenues for the six months ended June 30, 2016 decreased by approximately 10% to $472.0 million from $524.5 million in the same period of 2015, primarily due to lower pulp revenues.

Pulp revenues in the first half of 2016 decreased by approximately 11% to $428.7 million from $480.8 million in the same period of 2015 due to lower pulp sales realizations.

Energy and chemical revenues remained essentially flat at $43.3 million in the first half of 2016 compared to $43.7 million in the same period of 2015.

Pulp production decreased marginally to 716,257 ADMTs in the first half of 2016 from 721,490 ADMTs in the same period of 2015. We had annual maintenance downtime of 21 days (approximately 29,600 ADMTs) in the first half of 2016, compared to 25 days (approximately 39,800 ADMTs) in the first half of 2015.

We estimate that such maintenance downtime in the first half of 2016 adversely impacted our Operating EBITDA by approximately $20.6 million, comprised of approximately $15.2 million in direct out-of-pocket expenses and the balance in reduced production. Many of our competitors that report their financial results using IFRS capitalize their direct costs of maintenance downtime.

Pulp sales volumes remained essentially flat at 723,779 ADMTs in the first half of 2016 compared to 721,041 ADMTs in the same period of 2015.

In the first half of 2016, list prices for NBSK pulp declined from the same period of 2015, largely as a result of the stronger dollar and weakening hardwood pulp prices impacting NBSK pulp prices. Average list prices for NBSK pulp in Europe were approximately $795 per ADMT in the first half of 2016, compared to approximately $871 per ADMT in the same period of 2015. Average list prices for NBSK pulp in China and North America were approximately $603 per ADMT and $962 per ADMT, respectively, in the first half of 2016, compared to approximately $667 per ADMT and $988 per ADMT, respectively, in the same period of 2015.

Average pulp sales realizations decreased by approximately 11% to $586 per ADMT in the first half of 2016 from approximately $661 per ADMT in the same period last year, primarily due to lower list prices.

In the first half of 2016, the dollar weakened and, as at June 30, 2016, was approximately 2% and 6% lower versus the euro and Canadian dollar, respectively, compared to December 31, 2015. This resulted in a negative impact on our dollar-denominated cash balances and receivables. On average, the dollar was stronger than the Canadian dollar during the first half of 2016, compared to the first half of 2015, which reduced our Canadian dollar-denominated expenses. The net impact of foreign exchange increased our Operating EBITDA in the six months ended June 30, 2016 by approximately $1.4 million compared to the same period of 2015.

Costs and expenses in the first half of 2016 decreased by approximately 4% to $427.1 million from $447.0 million in the first half of 2015, primarily due to lower fiber prices and the reversal of a $7.2 million wastewater fee accrual at our Rosenthal mill.

In the first half of 2016, operating depreciation and amortization was $34.9 million, compared to $33.7 million in the same period of 2015.

Selling, general and administrative expenses decreased to $22.1 million in the first half of 2016 from $23.1 million in the same period of 2015.

Transportation costs decreased by approximately 11% to $33.3 million in the first half of 2016 from $37.4 million in the same period of 2015 primarily due to lower sales shipments from our Celgar mill resulting from its maintenance downtime and slow restart.

On average, in the first half of 2016 overall fiber prices decreased by approximately 7% from the same period of 2015, primarily as a result of a balanced wood market in both Germany and the Celgar mill s fiber basket. In the first half of 2016, in euro terms, average fiber prices in Germany were approximately 8% lower than the comparative period. In the first half of 2016, in Canadian dollar terms, average fiber prices for our Celgar mill were marginally lower than the comparative period.

In the first half of 2016, our operating income decreased by approximately 42% to $44.9 million from $77.5 million in the same period of 2015, primarily due to 11% lower pulp sales realizations, partially offset by lower fiber prices and the reversal of a wastewater fee accrual at our Rosenthal mill.

Interest expense in the first half of 2016 decreased to $25.9 million from $27.4 million in the same period of 2015, primarily as a result of lower indebtedness.

As a result of a weakening of the dollar versus the Canadian dollar in the first half of 2016, we recorded a non-cash gain on the foreign exchange translation of certain intercompany debt between Mercer Inc. and its wholly owned subsidiaries, which increased our net income by $0.3 million.

In the first half of 2016, we had a loss of $0.5 million due to the write-off of deferred financing costs associated with our repurchase and cancellation of $23.0 million of our 2019 Senior Notes.

During the first half of 2016, income tax expense decreased to $14.1 million from $15.2 million in the same period of 2015 due to lower taxable income for our German mills.

For the first half of 2016, we reported net income of $4.5 million, or $0.07 per basic and diluted share compared to net income of $30.0 million, or $0.47 per basic and $0.46 per diluted share, in the same period of 2015.

In the first half of 2016, Operating EBITDA decreased by approximately 28% to $80.1 million from $111.4 million in the same period of 2015, primarily as a result of lower pulp sales realizations, partially offset by lower fiber prices and the reversal of a wastewater fee accrual.

**Liquidity and Capital Resources**

***Summary of Cash Flows***

| | Six Months Ended June 30, | | | |
|---|---|---|---|---|
| | 2016 | | 2015 | |
| | (in thousands) | | | |
| Net cash provided by operating activities | $ | 74,743 | $ | 70,279 |
| Net cash used in investing activities | | (19,009) | | (20,364) |
| Net cash used in financing activities | | (44,787) | | (8,876) |
| Effect of exchange rate on changes in cash and cash equivalents | | 2,075 | | (3,344) |
| Net increase in cash and cash equivalents | $ | 13,022 | $ | 37,695 |

***Cash Flows from Operating Activities.*** We operate in a cyclical industry and our operating cash flows vary accordingly. Our principal operating cash expenditures are for labor, fiber and chemicals.

Working capital levels fluctuate throughout the year and are affected by maintenance downtime, changing sales patterns, seasonality and the timing of receivables and revenues and the payment of payables and expenses.

Cash provided by operating activities was $74.7 million in the six months ended June 30, 2016 and $70.3 million in the comparative period of 2015. A decrease in accounts receivable provided cash of $12.5 million in the six months ended June 30, 2016, compared to an increase in accounts receivable using cash of $22.7 million in the same period of 2015. A decrease in accounts payable and accrued expenses excluding non-cash items used cash of $0.1 million in the first half of 2016, compared to an increase in accounts payable and accrued expenses providing cash of $18.1 million in the same period of 2015. A decrease in inventories provided cash of $11.0 million in the first half of 2016, compared to an increase in inventories using cash of $5.6 million in the comparative period of 2015.

***Cash Flows from Investing Activities.*** Investing activities in the six months ended June 30, 2016 used cash of $19.0 million, primarily related to capital expenditures of $20.4 million, partially offset by a decrease in restricted cash of $1.6 million. In the first half of 2016, capital expenditures primarily related to new wood harvesting equipment and a logistics and reload facility for our Celgar mill, a rail acceptance system for logs and lime kiln retrofit at our Rosenthal mill and various other smaller projects. In the same period of 2015, investing activities used cash of $20.4 million.

***Cash Flows from Financing Activities.*** In the first half of 2016, financing activities used cash of $44.8 million, including $23.1 million to repurchase and cancel $23.0 million of our 2019 Senior Notes, $14.9 million for the payment of dividends and $5.9 million for a scheduled payment in respect of our interest rate derivative. In the same period of 2015, financing activities used cash of $8.9 million.

**Balance Sheet Data**

The following table is a summary of selected financial information as at the dates indicated:

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| | (in thousands) | |
| **Financial Position** | | |
| Cash and cash equivalents | $ 112,651 | $ 99,629 |
| Total current assets | $ 385,764 | $ 388,811 |
| Total current liabilities | $ 104,528 | $ 104,421 |
| Working capital | $ 281,236 | $ 284,390 |
| | | |
| Total assets | $ 1,180,269 | $ 1,182,817 |
| Debt | $ 616,492 | $ 638,043 |
| Total liabilities | $ 780,049 | $ 799,841 |
| Total equity | $ 400,220 | $ 382,976 |

As a result of the weakening of the dollar versus the euro and the Canadian dollar as at June 30, 2016, we recorded a non-cash increase in the carrying value of our net assets, consisting primarily of our fixed assets, denominated in euros and Canadian dollars. This non-cash increase of approximately $25.4 million does not affect our net income (loss), Operating EBITDA or cash flows but is reflected in our other comprehensive income (loss) and as an increase to our total equity.

***Sources and Uses of Funds***

Our principal sources of funds are cash flows from operations, cash and cash equivalents on hand and our revolving credit facilities. Our principal uses of funds consist of operating expenses, capital expenditures and semi-annual interest payments on our outstanding 7.0% Senior Notes due 2019 and 7.75% Senior Notes due 2022.

The following table sets out our total capital expenditures and interest expense for the periods indicated:

| | Six Months Ended June 30, | |
|---|---|---|
| | 2016 | 2015 |

| | | (in thousands) | | |
|---|---|---|---|---|
| Capital expenditures | $ | 20,415 | $ | 18,771 |
| Cash paid for interest[1] | $ | 24,635 | $ | 25,905 |
| Interest expense[2] | $ | 25,927 | $ | 27,360 |

(1) Amounts differ from interest expense which includes non-cash items. See supplemental disclosure of cash flow information from our Interim Consolidated Statement of Cash Flows included in this report.
(2) Interest on our 2019 Senior Notes and 2022 Senior Notes is paid semi-annually in June and December of each year.

In the first half of 2016, we expended $23.1 million to repurchase and cancel $23.0 million of our 2019 Senior Notes and $14.9 million to pay two quarterly dividends of $0.115 per common share each on January 5, 2016 and April 5, 2016, respectively.

As at June 30, 2016, our cash and cash equivalents had increased to $112.7 million from $99.6 million at the end of 2015 and our working capital had decreased marginally to $281.2 million from $284.4 million at the end of 2015.

As at June 30, 2016, we had approximately $137.7 million available under our revolving credit facilities.

As at June 30, 2016, we had no material commitments to acquire assets or operating businesses.

Based upon the current level of operations and our current expectations for future periods in light of the current economic environment, and in particular, current and expected pulp pricing and foreign exchange rates, we believe that cash flow from operations and available cash, together with available borrowings under our revolving credit facilities, will be adequate to finance the capital requirements for our business including the payment of our quarterly dividend during the next 12 months.

In the future we may make acquisitions of businesses or assets or commitments to additional capital projects. To achieve the long-term goals of expanding our assets and earnings, including through acquisitions, capital resources will be required. Depending on the size of a transaction, the capital resources that will be required can be substantial. The necessary resources will be generated from cash flow from operations, cash on hand, borrowing against our assets or the issuance of securities.

***Debt Covenants***

Certain of our long-term obligations contain various financial tests and covenants customary to these types of arrangements. See our annual report on Form 10-K for the fiscal year ended December 31, 2015.

As at June 30, 2016, we were in full compliance with all of the covenants of our indebtedness.

***Off-Balance Sheet Arrangements***

At June 30, 2016, we did not have any off-balance sheet arrangements (as defined in Item 303(a)(4)(ii) of Regulation S-K).

***Contractual Obligations and Commitments***

There were no material changes outside the ordinary course to any of our material contractual obligations during the six months ended June 30, 2016.

**Foreign Currency**

As a majority of our assets, liabilities and expenditures are held or denominated in euros or Canadian dollars, our consolidated financial results are subject to foreign currency exchange rate fluctuations.

We translate foreign denominated assets and liabilities into dollars at the rate of exchange on the balance sheet date. Equity accounts are translated using historical exchange rates. Unrealized gains or losses from these translations are recorded in other comprehensive income (loss) and do not affect our net earnings.

As a result of the weakening of the dollar versus the euro and Canadian dollar as at June 30, 2016, we recorded a non-cash increase of $25.4 million in the carrying value of our net assets, consisting primarily of our fixed assets, denominated in euros and Canadian dollars. As a result, our accumulated other comprehensive loss decreased to $145.6 million.

Based upon the exchange rate as at June 30, 2016, the dollar has weakened by approximately 2% and 6% in value against the euro and the Canadian dollar, respectively, since December 31, 2015. See Quantitative and Qualitative Disclosures about Market Risk .

**Critical Accounting Policies**

The preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect both the amount and the timing of the recording of assets, liabilities, revenues, and expenses in the consolidated financial statements and accompanying note disclosures. Our management routinely makes judgments and estimates about the effects of matters that are inherently uncertain. As the number of variables and assumptions affecting the probable future resolution of the uncertainties increases, these judgments become even more subjective and complex.

Our significant accounting policies are disclosed in Note 1 to our audited annual financial statements included in our annual report on Form 10-K for the fiscal year ended December 31, 2015. While all of the significant accounting policies are important to the consolidated financial statements, some of these policies may be viewed as having a high degree of judgment. On an ongoing basis using currently available information, management reviews its estimates, including those related to accounting for, among other things, pension and other post-retirement benefit obligations, deferred income taxes (valuation allowance and permanent reinvestment), depreciation and amortization, future cash flows associated with impairment testing for long-lived assets, legal liabilities and contingencies. Actual results could differ materially from these estimates, and changes in these estimates are recorded when known.

We have identified certain accounting policies that are the most important to the portrayal of our current financial condition and results of operations.

For information about both our significant and critical accounting policies, see our annual report on Form 10-K for the fiscal year ended December 31, 2015.

**Cautionary Statement Regarding Forward-Looking Information**

The statements in this report that are not reported financial results or other historical information are forward-looking statements within the meaning of the *Private Securities Litigation Reform Act of 1995*, as amended.

Generally, forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. They often include words such as expects , anticipates , intends , plans , believes , seeks , es words of similar meaning, or future or conditional verbs, such as will , should , could , or may , although not forward-looking statements contain these identifying words. Forward-looking statements are based on expectations, forecasts and assumptions by our management and involve a number of risks, uncertainties and other factors, many of which are beyond our control, that could cause actual conditions, events or results to differ significantly from those described in the forward-looking statements. These factors include, but are not limited to, the following:

- our business is highly cyclical;
- a weakening of the global economy, including capital and credit markets, could adversely affect our business and financial results and have a material adverse effect on our liquidity and capital resources;
- our level of indebtedness could negatively impact our financial condition, results of operations and liquidity;
- cyclical fluctuations in the price and supply of our raw materials, particularly fiber, could adversely affect our business;
- we face intense competition in our markets;
- we are exposed to currency exchange rate fluctuations;
- we are subject to extensive environmental regulation and we could incur substantial costs as a result of compliance with, violations of or liabilities under applicable environmental laws and regulations;
- our business is subject to risks associated with climate change and social and government responses thereto;
- our new ERP system may cost more than expected, be delayed, fail to perform as planned and interrupt operational transactions during and following the implementation, which could adversely affect our operations and results of operations;
- we periodically use derivatives to manage certain risks which has caused significant fluctuations in our operating results;

our operations require substantial capital and we may be unable to maintain adequate capital resources to provide for such capital requirements;

future acquisitions may result in additional risks and uncertainties in our business;

changes in credit ratings issued by nationally recognized statistical rating organizations could adversely affect our cost of financing and have an adverse effect on the market price of our securities;

we rely on government grants and participate in German statutory energy programs;

we are subject to risks related to our employees;

we are dependent on key personnel;

we may experience material disruptions to our production (including as a result of, among other things, planned and unplanned maintenance downtime);

if our long-lived assets become impaired, we may be required to record non-cash impairment charges that could have a material impact on our results of operations;

we may incur losses as a result of unforeseen or catastrophic events, including the emergence of a pandemic, terrorist attacks or natural disasters;

our insurance coverage may not be adequate;

we rely on third parties for transportation services;

failures or security breaches of our information technology systems could disrupt our operations and negatively impact our business;

the price of our common stock may be volatile;

a small number of our shareholders could significantly influence our business;

our international sales and operations are subject to applicable laws relating to trade, export controls and foreign corrupt practices, the violation of which could adversely affect our operations; and

we are exposed to interest rate fluctuations.

Given these uncertainties, you should not place undue reliance on our forward-looking statements. The forgoing review of important factors is not exhaustive or necessarily in order of importance and should be read in conjunction with the risks and assumptions including those set forth in reports and other documents we have filed with or furnished to the SEC, including in our annual report on Form 10-K for the fiscal year ended December 31, 2015. We advise you that these cautionary remarks expressly qualify in their entirety all forward-looking statements attributable to us or persons acting on our behalf. Unless required by law, we do not assume any obligation to update forward-looking statements based on unanticipated events or changed expectations. However, you should carefully review the reports and other documents we file from time to time with the SEC.

**Cyclical Nature of Business**

***Revenues***

The pulp business is highly cyclical in nature and markets are characterized by periods of supply and demand imbalance, which in turn can materially affect prices. Pulp markets are sensitive to cyclical changes in the global economy, industry capacity and foreign exchange rates, all of which can have a significant influence on selling prices and our operating results. The length and magnitude of industry cycles have varied over time but generally reflect changes in macro-economic conditions and levels of industry capacity. Pulp is a commodity that is generally available from other producers. Because commodity products have few distinguishing qualities from producer to producer, competition is generally based upon price, which is generally determined by supply relative to demand.

Industry capacity can fluctuate as changing industry conditions can influence producers to idle production capacity or permanently close mills. In addition, to avoid substantial cash costs in idling or closing a mill, some producers will choose to operate at a loss, sometimes even a cash loss, which can prolong weak pricing environments due to oversupply. Oversupply of our products can also result from producers introducing new capacity in response to favorable pricing trends. Certain integrated pulp and paper producers have the ability to discontinue paper production by idling their paper machines and selling their NBSK pulp production on the market, if market conditions, prices and trends warrant such actions.

Demand for pulp has historically been determined primarily by general global macroeconomic conditions and has been closely tied to overall business activity. NBSK pulp prices have been and are likely to continue to be volatile and can fluctuate widely over time. Between 2005 and 2015, European list prices for NBSK pulp have fluctuated between a low of approximately $575 per ADMT in 2009 to a high of $1,030 per ADMT in 2011.

A producer s actual pulp sales realizations are list prices net of customer discounts, rebates and other selling concessions. Over the last three years, these have increased as producers compete for customers and sales. Our pulp sales realizations may also be affected by NBSK price movements between the order and shipment dates.

Accordingly, prices for pulp are driven by many factors outside our control, and we have little influence over the timing and extent of price changes, which are often volatile. Because market conditions beyond our control determine the price for pulp, prices may fall below our cash production costs, requiring us to either incur short-term losses on product sales or cease production at one or more of our mills. Therefore, our profitability depends on managing our cost structure, particularly raw materials which represent a significant component of our operating costs and can fluctuate based upon factors beyond our control. If the prices of our products decline, or if prices for our raw materials increase, or both, our results of operations and cash flows could be materially adversely affected.

***Costs***

Our production costs are influenced by the availability and cost of raw materials, energy and labor, and our plant efficiencies and productivity. Our main raw material is fiber in the form of wood chips and pulp logs. Wood chip and pulp log costs are primarily affected by the supply of, and demand for, lumber and pulp, which are both highly cyclical. Over the last three years, the demand and competition for fiber has also been impacted by renewable energy producers in Germany, particularly by wood pellet producers. Higher fiber prices could affect producer profit margins if they are unable to pass along price increases to pulp customers or purchasers of surplus energy.

***Currency***

We have manufacturing operations in Germany and Canada. Most of the operating costs and expenses of our German mills are incurred in euros and those of our Celgar mill in Canadian dollars. However, the majority of our sales are in products quoted in dollars. Our results of operations and financial condition are reported in dollars. As a result, our costs generally benefit from a strengthening dollar but are adversely affected by a decrease in the value of the dollar relative to the euro and to the Canadian dollar. Such shifts in currencies relative to the euro and the Canadian dollar reduce our operating margins and the cash flow available to fund our operations and to service our debt. This could have a material adverse effect on our business, financial condition, results of operations and cash flows.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risks from changes in interest rates and foreign currency exchange rates, particularly the exchange rates between the U.S. dollar and the euro and Canadian dollar. Changes in these rates may affect our results of operations and financial condition and, consequently, our fair value. We seek to manage these risks through internal risk management policies as well as the periodic use of derivatives. We may use derivatives to reduce or limit our exposure to interest rate, currency and pulp price risks. We use derivatives to reduce our potential losses or to augment our potential gains, depending on our management s perception of future economic events and developments. These types of derivatives are generally highly speculative in nature. They are also very volatile as they are highly leveraged given that margin requirements are relatively low in proportion to notional amounts.

For additional information, please refer to Part II, Item 7A. Quantitative and Qualitative Disclosures about Market Risk included in our annual report on Form 10-K for the fiscal year ended December 31, 2015.

We record unrealized gains and losses on our outstanding derivatives when they are marked to market at the end of each reporting period and realized gains or losses on them when they are settled. We determine market valuations based primarily upon valuations provided by our counterparties.

During the first half of 2016, we recorded a derivative loss of approximately $0.3 million on our outstanding interest rate derivative, compared to a derivative loss of approximately $0.4 million in the same period of 2015.

## ITEM 4. CONTROLS AND PROCEDURES

**Disclosure Controls and Procedures**

Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the *Securities Exchange Act of 1934*, as amended, referred to as the Exchange Act ), as of the end of the period covered by this report. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Based on such evaluation, our principal executive officer and principal financial officer have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act.

It should be noted that any system of controls is based in part upon certain assumptions designed to obtain reasonable (and not absolute) assurance as to its effectiveness and there can be no assurance that any design will succeed in achieving its stated goals.

**Changes in Internal Controls**

There have been no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

We are subject to routine litigation incidental to our business, including that which is described in our latest annual report on Form 10-K for the fiscal year ended December 31, 2015. We do not believe that the outcome of such litigation will have a material adverse effect on our business or financial condition.

### ITEM 1A. RISK FACTORS

As of June 30, 2016, there have been no material changes to the factors disclosed in Item 1A. Risk Factors in our latest annual report on Form 10-K for the fiscal year ended December 31, 2015.

### ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

### ITEM 4. MINE SAFETY DISCLOSURES

None.

### ITEM 5. OTHER INFORMATION

None.

**ITEM 6. EXHIBITS**

| Exhibit No. | Description |
|---|---|
| 31.1 | Section 302 Certification of Chief Executive Officer |
| 31.2 | Section 302 Certification of Chief Financial Officer |
| 32.1* | Section 906 Certification of Chief Executive Officer |
| 32.2* | Section 906 Certification of Chief Financial Officer |
| 101 | The following financial statements from the Company s Form 10-Q for the fiscal period ended June 30, 2016, formatted in XBRL: (i) Interim Consolidated Statements of Operations; (ii) Interim Consolidated Statements of Comprehensive Income (Loss); (iii) Interim Consolidated Balance Sheets; (iv) Interim Consolidated Statements of Cash Flows; and (v) Notes to Interim Consolidated Financial Statements. |

* In accordance with Release No. 33-8212 of the SEC, these Certifications: (i) are furnished to the SEC and are not filed for the purposes of liability under the Securities Exchange Act of 1934, as amended; and (ii) are not to be subject to automatic incorporation by reference into any of the Company s registration statements filed under the Securities Act of 1933, as amended, for the purposes of liability thereunder or any offering memorandum, unless the Company specifically incorporates them by reference therein.

## SIGNATURES

Pursuant to the requirements of the *Securities Exchange Act of 1934*, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**MERCER INTERNATIONAL INC.**

By: /s/ David M. Gandossi
David M. Gandossi
Chief Executive Officer and President

Date: July 28, 2016